



## STATE BOARD OF EQUALIZATION STAFF LEGISLATIVE BILL ANALYSIS

Date Amended:	<b>05/17/04</b>	Bill No:	<b>AB 2106</b>
Tax:	<b>Sales and Use</b>	Author:	<b>Ridley-Thomas</b>
Board Position:		Related Bills:	

### BILL SUMMARY

This bill would, among other things, require the Department of Finance (DOF) to submit to the Legislature a report of tax expenditures currently in effect. The bill would specify that, among other things, based on information provided by the Board to the extent feasible, the report include the number of tax returns or taxpayers affected by any sales or use tax expenditure, the distribution of that expenditure, and the size and type of business or industry to which that expenditure is made available.

### ANALYSIS

#### Current Law

Under current law, pursuant to Section 13305 of the Government Code, the Department of Finance has been required to provide a tax expenditure report to the Legislature since 1971. Chapter 1762, Statutes of 1971, required that the report be submitted to the Legislature once every two years. Chapter 268, Statutes of 1984, increased the reporting frequency to once a year. The required report includes each of the following:

- A comprehensive list of tax expenditures.
- Additional detail on individual categories of tax expenditures.
- Historical information on the enactment and repeal of tax expenditures.

#### Proposed Law

This bill would add Article 7.5 (commencing with Section 9147.1) to Chapter 1.5 of Part 1 of Division 2 of Title 2 of, and to repeal Section 13305 of, the Government Code to do, among other things, the following:

- 1) Define “tax expenditure” as a “credit, deduction, exclusion, exemption, or any other tax benefit as may be provided for by state law.”
- 2) Require the DOF to submit a tax expenditure report by September 15 each odd-numbered year starting in 2005, that would contain the following:
  - a) A description of each expenditure, its statutory authority, its intent, and the revenue loss under the Sales and Use Tax Law, the Personal Income Tax Law, and the Corporation Tax Law.
  - b) With respect to the sales and use tax expenditures that are separately identified on returns or claims, information on the number of returns or taxpayers affected, and the distribution of each tax expenditure. For business tax expenditures, information on the size, total receipts, and type of business, as provided by the Board to the extent feasible.

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The bill would require the Legislative Analyst's office to report to the Assembly and Senate Revenue and Taxation Committees addressing each tax expenditure, as specified.

In addition, the bill would require the Assembly and Senate budget committees to consider the Legislative Analyst's recommendations and require the Joint Legislative Budget Committee to review and prioritize recommendations made by the revenue and taxation committees.

The bill would additionally require any legislation establishing a new or expanded tax expenditure to contain a sunset provision, a requirement for evaluation study, recapture provisions, and measurable goals or objectives.

### In General

#### COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by the author. According to the author's office, the purpose of the bill is to provide for a systematic review of tax expenditures in order to determine their effectiveness.
2. **The Board does not have specific data on tax expenditures.** In general, revenue estimates and expenditure data for the Personal Income Tax and Corporation Tax Laws are easier to quantify than they are for the Sales and Use Tax Law. Personal income and corporation tax returns contain significant detail regarding different sources of income and types of exemptions, exclusions, deductions, and credits claimed. Thus, tax return data are often available when estimating the fiscal impact of various income and corporate tax expenditure programs. In contrast, returns filed by taxpayers under the Sales and Use Tax Law (a copy of which is attached) contain little specific information regarding tax expenditures.

As shown on the attached sales and use tax return, some of the more common tax expenditures allowed under the Sales and Use Tax Law are separately identified on the return itself for purposes of allowing taxpayers to claim the deduction. These include deductions for, among others, sales for resale, sales to the U.S. Government, sales in interstate or foreign commerce, food products, and nontaxable labor deduction (note, the law contains numerous other tax exemptions and exclusions not separately identified on the return). However, instead of actually itemizing these deductions, many taxpayers simply report their taxable sales, netting out any exempt sales. Consequently, return information does not capture specific data on the myriad of tax exemptions and exclusions provided under the law, and is not a reliable source to use in making estimates of revenue losses attributable to those exemptions and exclusions. Consequently, the Board generally relies on independent data sources when estimating the revenue impacts of various sales tax expenditure programs.

The exception to this is for partial exemptions. The Board currently requires the taxpayer to specify the amount of those exemptions that apply to only a portion of the combined state and local sales and use tax. There are currently five such exemptions in effect:

Teleproduction Equipment

Farm Equipment

Diesel Fuel Used in Farming and Food Processing

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Timber Harvesting Equipment and Machinery  
Racehorse Breeding Stock

These commodities are exempt from the *state* sales and use tax. Local and special district sales and use taxes continue to apply. In order for a taxpayer to claim these exemptions, they must report the amount of the transactions that are subject to the partial exemption.

Consequently, since the bill specifies that the Board would provide the information to the extent feasible, it is assumed that the Board would provide the DOF with the information we are currently capturing.

### **COST ESTIMATE**

As explained previously, the Board does not capture reliable data on tax expenditures from tax returns or from taxpayers, other than that obtained on the five partial tax exemptions. The bill states that the DOF would prepare the report with information from the Board to the extent feasible. It is assumed that the Board would provide the DOF information that we currently obtain from returns. Based on that assumption, any costs associated with this measure would be insignificant.

### **REVENUE ESTIMATE**

To the extent that future reviews and evaluations result in the identification and termination of ineffective or inappropriate tax expenditures, enactment of this measure could result in unknown additional revenues.

### **ATTACHMENT**

<http://www.boe.ca.gov/pdf/boe401a2.pdf>

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